



APPLYING VAT TO PRIVATE SCHOOL FEES

Issued 13 September 2024

ICAEW welcomes the opportunity to comment on the Applying VAT to Private School Fees and Removing the Business Rates Charitable Rates Relief for Private Schools Technical Note published by HM Treasury on 29 July 2024, a copy of which is available from this [link](#). However, we note that our own process for preparing a response has been limited by the consultation period being significantly shorter than the 12 weeks recommended by the Cabinet Office in its [consultation principles](#).

This response of 13 September 2024 has been prepared by the ICAEW Tax Faculty. Internationally recognised as a source of expertise, the ICAEW Tax Faculty is a leading authority on taxation and is the voice of tax for ICAEW. It is responsible for making all submissions to the tax authorities on behalf of ICAEW, drawing upon the knowledge and experience of ICAEW's membership. The Tax Faculty's work is directly supported by over 130 active members, many of them well-known names in the tax world, who work across the complete spectrum of tax, both in practice and in business. ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark the tax system and changes to it, are summarised in Appendix 1.

ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision of a world of strong economies, ICAEW works with governments, regulators and businesses and it leads, connects, supports and regulates more than 169,000 chartered accountant members in over 146 countries. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical and ethical standards.

© ICAEW 2024

All rights reserved.

This document may be reproduced without specific permission, in whole or part, free of charge and in any format or medium, subject to the conditions that:

- it is appropriately attributed, replicated accurately and is not used in a misleading context;
- the source of the extract or document is acknowledged and the title and ICAEW reference number are quoted.

Where third-party copyright material has been identified application for permission must be made to the copyright holder.

For more information, please contact: taxfac@icaew.com

ICAEW

Chartered Accountants' Hall Moorgate Place London EC2R 6EA UK
icaew.com

The Institute of Chartered Accountants in England and Wales (ICAEW) incorporated by Royal Charter (RC000246)
Registered office: Chartered Accountants' Hall Moorgate Place London EC2R 6EA UK

KEY POINTS

1. As well as seeking input from VAT specialists from our membership regarding the draft legislation, we have also received comments from members who have experience working within the finance teams of private schools on the practical application of the legislation.
2. While we have answered below the specific questions from the technical note, we consider there to be a number of more serious concerns regarding this policy change.
3. In many cases, these are not concerns with the draft legislation itself, but practical issues caused by the legislation that we believe need to be considered in more detail.
4. Most of these issues are not insurmountable from a VAT perspective. However, we consider that implementing this legislation with effect from 1 January 2025 does not give private schools sufficient time to prepare for the change. We also have concerns about making this change part way through an academic year.
5. We would therefore strongly recommend that the government considers making the change so that it instead applies to terms starting, say, on or after 1 August 2025.
6. We have provided more detail in the body of our representation but note some practical issues below, all of which could be resolved if the application of VAT took effect for terms starting on or after 1 August 2025:
 - a. Many independent schools will not currently be VAT-registered and will be required to register before 1 January 2025. This could place unnecessary strain on HMRC and might not give those schools sufficient time to seek professional advice regarding their registration.
 - b. Schools that are not currently VAT-registered are unlikely to have their accounting systems set up to comply with VAT and may need to update their accounting systems before January. This is a very short timeframe for such a project and could therefore lead to poor VAT compliance in the early months of this change.
 - c. Fee schedules for the 24/25 academic year will in most cases have been sent out around Easter 2024, before the general election. Although fee increases may be possible with at least one term's notice, many schools will be required to absorb the VAT cost for the spring term. Where schools are able to increase fees for the summer term, this could lead to parents seeking to move their child to a state school part way through the academic year, which most importantly is likely to be detrimental for the child, but will also cause problems for the private school and for the state school system.
7. Again, more detail is provided below, but we have also identified the following VAT issues with the draft legislation:
 - a. The definition of private school potentially catches some institutions that it does not intend to catch, such as:
 - i. Some nursery schools, which may have one or more compulsory school age children;
 - ii. Some sixth forms that are in a similar position to Colchester Institute Corporation, see Upper Tribunal case *Colchester Institute Corporation vs HMRC [2020] UKUT 0368 (TCC)*; and
 - iii. Some universities, which may provide full-time education to students under the age of 19.
 - b. The “connected persons” test may not catch all possible arrangements to avoid the VAT charge.
 - c. The decision to keep other “closely related” goods and services other than boarding exempt from VAT is likely to cause legislative and administrative issues, and we do not

necessarily agree that the risk of schools inflating the values of exempt elements of their supply to be “low”. Even where the inflation is not deliberate, this approach is likely to cause valuation issues.

- d. The decision not to restrict VAT recovery under the Capital Goods Scheme is, on VAT principles, the right one, but could lead to fairly significant VAT reclaims.

ANSWERS TO SPECIFIC QUESTIONS

Question 1: Does the above definition of private schools capture all private schools across the UK?

8. The definition states that a “private school” means
- a. *either*
 - i. *a school at which full-time education is provided for pupils of compulsory school age or, in Scotland, school age (whether or not such education is also provided for pupils under or over that age), or*
 - ii. *an institution at which full-time education is provided for persons over compulsory school age but under 19 and which is principally concerned with providing education suitable to the requirements of such persons (for example, a sixth form college), and*
 - b. *where fees or other consideration are payable for that provision of full-time education.*
9. Some members expressed a concern that this definition appears to preclude institutions where education is provided for persons who are *not* under the age of 19. There are a number of reasons why pupils may be 19 or older but still attending a private school sixth form, sixth form college or further education college, for example, if they have been held back a year for educational reasons.
10. Although we note that the definition does not state that the education must be *solely* provided to persons over compulsory school age but under 19, we recommend that the position is clarified.
11. One member raised that the Education Act 1996 states at Section 2(5) that ‘*where a person has begun a particular course of secondary education before attaining the age of 18, and continues to attend that course, the education does not cease to be secondary education by reason of his having attained the age of 19.*’ It was suggested that the two definitions could be aligned.
12. There were differing views among our membership about whether the example (‘a sixth form college’) was a helpful addition to the legislation. It was noted that if the legislation is comprehensively drafted, examples should not be needed; examples may only provide greater certainty to taxpayers where they are part of an exhaustive list.

Question 2: Does this definition inadvertently capture any organisations that this policy does not intend to capture?

Nursery schools

13. Item 1 of the draft legislation states that “the provision of education by a private school, other than the provision of education in a nursery class” will be standard-rated as an exception to the exemption.
14. Note 5 states that “for the purposes of item 1, a “nursery class” means a class that is composed wholly of children who are under compulsory school age or, in Scotland, school age, and would not be expected to attain that age while in that class.”

15. Where parents [request admission out of the normal age group](#), the child is likely to stay in a nursery class even though they are, or become, of compulsory school age during the academic year.
16. On the face of it, because the draft legislation does not state that the education has to be *solely* provided to pupils of compulsory school age, the draft legislation appears to have the effect that any nursery class with a child of compulsory school age in it will not be a “nursery class” for the purposes of the VAT legislation and the fees for the entire class will become standard-rated where provided by a private school.
17. We have concerns that not only might this capture nursery classes attached to private schools, which itself goes against the aims of the legislation, but that standalone nursery schools could also be caught. We recommend that this is considered in more detail.
18. In practice, nurseries may choose to not accept children of compulsory school age going forward. It is not clear where these children will then be educated.
19. However, for the 24/25 academic year, schools in this position may be forced to absorb the VAT charge for terms starting on or after 1 January 2025 where their nursery class has a child of compulsory school age.
20. Furthermore, we note that many private schools will have both nursery classes and reception classes. In many cases, these classes might have shared activities and will often use shared facilities. Where the classes overlap, it is not clear how this will affect the exemption position but at the very least, it will cause additional partial exemption problems for schools in that position.

Sixth forms

21. Members have also expressed concern that some school sixth forms, sixth form colleges or further education colleges could be caught by the definition included within the draft legislation, particularly in light of the Upper Tribunal case *Colchester Institute Corporation vs HMRC [2020] UKUT 0368 (TCC)*.
22. In the Colchester Institute Corporation case, the Upper Tribunal examined whether the provision of free education and vocational training, funded by government grants, constituted a “supply of services for consideration” for VAT purposes. The Tribunal concluded that it did, emphasising the direct link between the government funding and the educational services provided, even though the funding wasn’t tied to specific students or courses.
23. This decision has raised concerns that the draft legislation’s definition of “private school” might be broader than intended, potentially encompassing institutions like school sixth forms, sixth form colleges, and further education colleges that receive government funding and would not traditionally be viewed as “private schools.”

Universities

24. We note that a private school is defined as “an institution at which full-time education is provided for persons over compulsory school age but under 19, and which is principally concerned with providing education suitable to the requirements of such persons (for example, a sixth form college), and (b) where fees or other consideration are payable for that provision of full-time education.”
25. We have concerns that the term “institution” is not defined, which could inadvertently catch universities. Most students are 18 when they start university, though some may be as young as 17, particularly those from the Scottish school system. University students are generally considered to be in full-time education, and fees are typically payable for this provision.
26. It may be that universities are excluded on the basis that they are not “principally concerned with providing education to the requirements of” students under the age of 19. However, we recommend that universities be explicitly excluded from the exception to the exemption, as we understand it is not the government’s intention to make university fees liable to VAT.

Question 3: Does the above “connected persons” test capture the relationships that exist between private schools and third parties?

27. We understand the “connected persons” test’ to refer to Note 2 of the draft legislation, which is as follows:
28. *For the purposes of items 1 and 2, the provision of education or vocational training at a private school by any eligible body other than a private school is to be treated as provision by a private school if*
 - a. *the eligible body and the private at which the provision is made are closely bound to one another by financial, economic and organisational links,*
 - b. *the eligible body and that private school are connected within the meaning of section 1122 of the Corporation Tax Act 2010 (connected persons), or*
 - c. *the provision by the eligible body is a result of arrangements the main purpose, or one of the main purposes, of which is to secure that the provision is an exempt supply.*
29. We have been made aware of private schools considering arrangements whereby self-employed teachers will be engaged directly by parents, seemingly allowing the teachers’ services to remain exempt as the supply of private tuition, or not subject to VAT as their taxable turnover would remain under the VAT registration threshold. Although there are a number of non-VAT reasons why this might not be feasible in practice, it does not appear that the connected persons test would capture such an arrangement.
30. It may be more practical for a separate trust to be set up to employ the teachers at the school. On the face of it, this could be an eligible body that is not connected within the meaning of section 1122 of the Corporation Tax Act 2010.
31. Although it seems likely that HMRC would argue that the eligible body and the private school in such a scenario would be closely bound by financial, economic and organisational links, this is a subjective test and the existence of these links would probably need to be determined by the courts.
32. Even if it were determined that the eligible body in this scenario was not connected to the private school by Note(2)(a) or (2)(b), we understand that Note(2)(c) should catch such an arrangement as the main purpose of it would be to secure an exempt supply. However, we consider there is a risk that a not-for-profit trust could attempt to argue that its activities are non-business and therefore outside the scope of VAT, rather than exempt, in which case Note(2)(c) would not activate.
33. We therefore recommend this part of the legislation is strengthened to ensure it captures all possible avoidance arrangements.
34. We also note that the connected persons test is only for the purposes of Items 1 and 2 and so does not apply to board and lodging. We understand that Item 3 means that board and lodging is otherwise caught by the standard rate where it is closely related to a supply falling within item 1 and 2.
35. It is not clear, however, whether the [reduced value rule](#) will apply to board and lodging, and if not, whether it could be applied through the supply of board and lodging through a connected person operating a “hotel”.

Question 4: Does this “connected persons” test inadvertently capture any relationships that it is not intended to capture?

36. We are not aware of any relationships this connected persons test might inadvertently capture that it is not intended to capture.

Question 5: Does this approach achieve the intended policy aims across all four UK nations?

37. Regarding VAT only, the approach appears to achieve the intended policy aims across all four UK nations.

OTHER COMMENTS ON THE DRAFT LEGISLATION

Implementation

38. Historically, many schools will not have had to account for VAT in their records so implementing this change will be significant, even without factoring in some of the additional complications referred to below.
39. Even for those schools that have had reason to be registered for VAT historically, it will be a significant change implementing the VAT changes in their accounting software. Most businesses would normally have at least 12 months planning for such a change.
40. We would suggest therefore that a longer pre-implementation period would be beneficial for schools affected by the change.
41. We note that most private schools will already have set their fees for the 24/25 academic year and will have published their fee schedules prior to the general election being called. In most cases, these schools will be required to give at least one full term's notice of an increase in fees. This means that the school may only be able to increase the fees for the summer term and, similarly, this will be when most parents first have the opportunity to remove their child from the private school.
42. This could lead to an influx of applications and admissions to state schools. We understand that state school funding is based on a census day that takes place in the autumn, which then determines the funding for 1 April onwards (in line with the government's financial year, rather than the academic year). If there is an influx of pupils at state schools in the summer term, it could therefore be a year before they receive the funding for the additional pupils.
43. We recommend delaying the introduction of VAT on private school fees so that it affects terms starting, say, on or after 1 August 2025 so that, where necessary, pupils can move schools between academic years and state school funding can be allocated accordingly.

Capital Goods Scheme

44. We note that the legislation does not restrict the use of the Capital Goods Scheme to recover VAT incurred in the past ten years (for land and property) on capital items that will now either be used for taxable purposes where they were not before or used for a higher percentage of taxable purposes than previously.
45. We assume this omission from the draft legislation is intentional. From a VAT principles perspective, we agree that it is appropriate for Capital Goods Scheme adjustments to be made where schools are now making taxable supplies.
46. However, we caution that this could lead to significant VAT reclaims from schools under the Capital Goods Scheme for investments in the purchase, construction, or refurbishment of land and property within the last ten years.
47. As noted above, many schools have not historically accounted for VAT, and most will not have separated out input VAT in their records. This will likely make it very difficult for them to claim historic VAT incurred and will probably involve a manual search through their accounting records.
48. Where no VAT was previously recovered on these assets, the assets were likely accounted for and depreciated on a VAT-inclusive basis. This will probably need adjusting, which might also have a direct tax impact.

Goods and services closely related to education

49. We note that other "closely related" goods and services other than boarding (i.e. goods and services that are provided by a private school for the direct use of their pupils and that are necessary for delivering the education to their pupils) will remain exempt from VAT.
50. We have a number of concerns regarding this approach. Firstly, from a practical perspective, it will be very difficult for schools to manage the bundled nature of the service.

51. There is a particular concern regarding the 24/25 academic year as fees will already have been set and, in some cases, paid. One member who has experience as a Finance Director in an independent school noted that: “Most fee schedules are published in the Easter before the start of the school year as most school T&Cs require a one term notice period from pupils (and fees are considered a key level in this decision-making process for parents). Fee schedules were all therefore communicated pre general election.”
52. It’s therefore not clear how schools will respond to being required to charge VAT on certain elements of a fee that has already been set (and possibly paid).
53. Even going forward, however, the valuation of different elements of the supply will not be straightforward. The Technical Note states that the Treasury considers the risk of value shifting to be low, but even where this might not be deliberate, this is likely to cause disputes between schools and HMRC regarding the valuation of certain elements.
54. While it may be relatively straightforward, at least in principle, to assign a reasonable value to items such as books, school meals, or transport, the valuation of extra-curricular activities, such as sports clubs that operate before and/or after school, presents a different challenge. These activities are typically included in the overall school fees. When these activities are conducted by school employees, can the VAT component of the fees be apportioned based on the time spent by staff? In addition, would a homework club be considered education or an extra-curricular activity?
55. We also have concerns regarding the legal status of these supplies. It is unclear how certain supplies, such as school meals, books, and transport (as mentioned in the Technical Note), can be exempt as ancillary to a supply of education that is now taxable. This seems to complicate an already complex area of VAT legislation and potentially overturns many years of established case law.
56. While we acknowledge that this decision has been made by the government, it would be significantly simpler from an administrative perspective if these “ancillary” supplies were not excluded from the exemptions. Additionally, although the Technical Note indicates that the government considers the risk of schools artificially inflating the value of these exempt supplies (value shifting) to be low, the risk of avoidance would be much lower if these supplies were also taxable.
57. On a separate note, it’s not clear why a supply of books (and potentially some supplies of transport) would not be zero-rated rather than exempt, as stated paragraph 2.13 of the Technical Note.
58. In addition, the Technical Note states in paragraph 2.18 that “the hiring out of facilities by a private school to a third-party has always been subject to VAT (if the school was VAT-registered). This will not change as a result of this policy.” This is misleading. If the letting is of [sports facilities](#), there are specific rules regarding this, and if it is the hire of a hall (for example), an option to tax would need to be in place for the letting to be taxable. Although this has no impact on the draft legislation, the Technical Note is a document of public record and should be accurate.

APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see <https://goo.gl/x6UjJ5>).